The Pakistan Credit Rating Agency Limited

Rating Report

Prosperity Weaving Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Sep-2020	A-	A2	Stable	Maintain	-
28-Sep-2019	A-	A2	Stable	Maintain	-
30-Mar-2019	A-	A2	Stable	Maintain	-
28-Dec-2018	A-	A2	Stable	Maintain	-
30-Jun-2018	A-	A2	Stable	Maintain	-
28-Dec-2017	A-	A2	Stable	Maintain	-
15-Jun-2017	A-	A2	Negative	Maintain	-
29-Dec-2016	A-	A2	Negative	Maintain	-
29-Dec-2015	A-	A2	Negative	Maintain	-
29-Dec-2014	A-	A2	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Prosperity Weaving Mills Limited, incorporated in 1991, is a part of one of the oldest medium-sized textile group in Pakistan - Nagina Group. The ratings reflect modest business profile of Prosperity Weaving; characterized by stable revenue, along with moderate margins. Prosperity Weaving’s topline dampened during 9MFY20; a resultant of lower production. The Company is adding 36 new looms to the capacity; to boost operational efficiency and achieve higher production volumes in the coming financial year. Prosperity Weaving caters to the need of local industry as well as export markets. However, the Company's operations came to a halt for an entire week during the last quarter of FY20, on account of the outbreak of COVID-19. The entire textile chain suffered due to lockdowns in Pakistan and internationally. Production resumed on 7th April,2020; since the Government allowed export-oriented sector to recommence operations. The financial profile of the Company is represented by lean working capital cycle; healthy coverages; and high leveraging - emanating from BMR/Expansion related borrowing. Nevertheless; the larger portion of long term debt was borrowed at SBP's concessionary rates, which was immensely favorable for the Company. The Company is exposed to market risk as exhibited by the impact of pandemic induced volatility in the stock market; which resulted in lackluster portfolio performance during 9MFY20. Any significant decline in investments leading to losses, and eventually equity erosion, will have an impact on the financial profile of the Company. The management’s ability to manage this risk is critical. In order to relieve pressure on cashflows caused by the pandemic- led economic slowdown, the Company availed SBP's moratorium relief and deferred principal repayments for one year. Reduction of 625bps in interest rates by SBP shall also provide respite in this regard. The demand for textile products is beginning to recover, as some major economies around the world reopen; while a few others are still observing vigilance to tackle an expected second wave of pandemic. The assigned ratings derive comfort from Prosperity Weaving's association with Nagina Group.

The ratings are dependent upon sustained market position of the Company. Moreover, the Company’s ability to generate enough cash flows to fulfill its financial obligations is critical, along with prudent investment decisions.

Disclosure

Name of Rated Entity	Prosperity Weaving Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Weaving(Sep-20)
Rating Analysts	Adil Kaleem | adil.kaleem@pacra.com | +92-42-35869504

Profile

Legal Structure Prosperity Weaving Mills Limited (Prosperity Weaving) was incorporated on November 20, 1991 as a public limited company.

Background Prosperity Weaving is associated with Nagina Group since its inception. The group has presence in spinning sector through Ellcot Spinning and Nagina Cotton. The Company's production facility is located in the vicinity of Sheikhupura.

Operations The Company's current operational capacity stands at 340 looms. The total energy requirement of the Company is ~5MW which is wholly met through captive plant. Furthermore, the Company has LESCO connection as an alternative source.

Ownership

Ownership Structure The majority stakes (~74%) of the Company is held by Nagina Group, through group companies and sponsoring individuals. The remaining shareholding rests with general public and financial institutions.

Stability The considerable positions in Nagina Group are held by Ellahi Family. The Group has a structured line of succession, reflected from equal distribution of shareholding among Ellahi brothers and their family members. Meanwhile, third generation has already been in business, serving at various capacities.

Business Acumen Nagina Group is one of the oldest medium-sized textile houses in Pakistan. Operating under Ellahi's for five decades, developing credential expertise in spinning and weaving over the period of time. The Group has adequately expanded its operations despite competitive textile industry.

Financial Strength Nagina Group comprises three listed public limited companies Ellcot Spinning Mills, Prosperity Weaving Mills and Nagina Cotton Mills Limited and six private limited companies. This portrays adequate financial strength of the Group to support the Company, if needed.

Governance

Board Structure Prosperity Weaving's board composition was increased to ten members during 9MFY20; out of which six members are non-executive directors, while one director carries the executive role and three are independent directors.

Members' Profile Mr. Shahzada Ellahi Shaikh – the Chairman – carries with him over two decades of experience in local textile industry. The board members have vast knowledge of textile industry; though diversity in experiences exists as well. The directors' expertise on different stages of the textile value-chain benefits the board in efficient decision making. During 9MFY20, Mr. Arfa Waheed Malik, Ms. Parveen Akhter Malik & Mr. Aneeq Khawar have joined as independent directors.

Board Effectiveness Three committees: Audit, Executive and Human Resource & Remuneration, are in place to assist the board in relevant matters and ensure proper oversight. Attendance of board members remains strong and meeting minutes were formally documented. Out of total, seven directors are Nagina Group nominees (including six sponsoring family individuals). Their dominance on board along with control over key management positions poses limited challenge to the management, thus, hampers effective governance.

Financial Transparency M/s. Deloitte Yousuf Adil, Chartered Accountants are the external auditors of the Company.

Management

Organizational Structure The management team is headed by Mr. Raza Ellahi Shaikh (CEO), with defined reporting line. The Company has five functional departments and all HOD's report directly to the CEO.

Management Team The management team is headed by the CEO Mr. Raza Ellahi who holds a graduate degree, in Economics. He is well verse with the textile business providing requisite acumen.

Effectiveness The management meetings are held on daily basis with follow-up points to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations. In addition to this, daily and weekly reports are generated for top management with main focus on production and liquidity position of the Company. Whereas, on monthly basis the Company's P&L is presented and discussed in the meetings.

MIS Prosperity Weaving has in place Oracle based Enterprise Resource Planning (ERP) system with comprehensive MIS reporting.

Control Environment The Company is compliant with multiple safety and quality assurance standard; including ISO 9001:2008, Global Organic Textile Standards and Organic Content Standard.

Business Risk

Industry Dynamics Textile exports of the country increased by ~14% for 1MFY21 to stand at ~USD 1.3bln as compared to ~USD 1.1bln in 1MFY20. Although the demand for textile products internationally deteriorated on account of lock downs in major export destinations, the export market had under-performed in 1MFY20. Furthermore, economies around the world have been gradually reopening as businesses recommenced in the past month. Hence, the exports in 1MFY21, experienced an upward trend despite prior lockdowns. Going forward, uncertainty still prevails with regards to full resumption of businesses around the globe and a return to normality. Locally, textile sector has found comfort in relief measures introduced by State Bank of Pakistan such as, deferment of loan payments for one year, low interest rates and salary refinance scheme.

Relative Position Prosperity Weaving is associated with Nagina Group. The Group has a long history of operations in Pakistan's spinning and weaving sectors. This strengthens the Company's market position. However, on standalone basis Prosperity weaving's share in local weaving industry is minimal.

Revenues Revenue of the Company reduced (9MFY20: 4,603mln; 9MFY19: PKR 5,112mln) on account of comparatively lower production due to lesser amount of looms operating when compared with same period last year. Sales mix remained unchanged, dominated by local sales and exports constituting ~25% (9MFY19: ~25%). The Company has concentration risk as its top customer accounted for more than 10% of the revenues in 9MFY20; however this top customer is considered one of the market leaders hence the risk is affordable.

Margins During 9MFY20, gross margin improved (9MFY20: 9.9%; 9MFY19: 8.4%) on account of better prices. This translated in to higher operating margin (9MFY20: 6.6%; 9MFY19: 5.6%). Net margin also recorded an increase (9MFY20: 3.9; 9MFY19: 1.7%), supplemented by reduced high finance cost (9MFY20: PKR 93mln; 9MFY19: PKR 132mln); resulting in a net income of PKR 178mln (9MFY19: PKR 88mln). The Company also has a small investment portfolio worth PKR 398mln, which includes equity investments as well as investment in mutual funds.

Sustainability Due to the lockdown enforced by the Government, the production had shut down for a week ending on 7th April, 2020; after which, the Company was partially operation. The pandemic had caused the demand to deteriorate around the world in the last quarter of FY20. However, off late, the demand has started to recover and sales are expected to bounce back. With the financial support schemes implemented by the Government, coupled with reduced policy rates by SBP, Prosperity Weaving is able to maneuver through the difficulties posed by the pandemic.

Financial Risk

Working Capital Net working capital cycle of the Company widened (9MFY20: 67 days; 9MFY19: 56 days) on account of increased inventory cycle (9MFY20: 34 days; 9MFY19: 27 days). Moreover, the room-to-borrow expanded (9MFY20: PKR 484mln; 9MFY19: PKR 178mln) on account of considerable reduction in short term borrowing (9MFY20: 493mln; 9MFY19: 1,018mln). This caused the short term trade leverage adequacy to improve significantly (9MFY20: ~44%; 9MFY19: ~13%).

Coverages During 9MFY20, free cash flows of the Company largely remained stagnant at PKR 423mln (9MFY19: PKR 428mln). However, the interest coverage increased considerably (9MFY20: 4.8x; 9MFY19: 3.4x), along with the debt coverage (9MFY20: 1.4x; 9MFY19: 1.3x); due to shrunken finance cost (9MFY20: PKR 93mln; 9MFY19: PKR 132mln).

Capitalization Prosperity Weaving has a highly leveraged capital structure. In 9MFY20, the leverage of the Company reduced to ~63% (9MFY19: ~71%), but still remained very high. This occurred on the back of lower total debt (9MFY20: PKR 1,963mln; 9MFY19: PKR 2,617mln). Out of the total,~25% consists of short term debt and ~55% was borrowed at SBP's concessionary rates.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Prosperity Weaving Mills Limited	Mar-20	Jun-19	Jun-18	Jun-17
Textile	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	2,032	2,240	2,248	2,273
2 Investments	398	445	451	549
3 Related Party Exposure	-	-	-	-
4 Current Assets	1,290	1,778	1,560	1,476
a Inventories	*639*	*520*	*358*	*386*
b Trade Receivables	*418*	*912*	*713*	*632*
5 Total Assets	3,720	4,463	4,260	4,299
6 Current Liabilities	452	494	429	437
a Trade Payables	*110*	*116*	*108*	*131*
7 Borrowings	1,963	2,694	2,730	2,787
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	137	120	100	107
10 Net Assets	1,168	1,155	1,001	968
11 Shareholders' Equity	1,168	1,155	1,001	968
B INCOME STATEMENT				
1 Sales	4,603	7,112	6,212	5,820
a Cost of Good Sold	*(4,145)*	*(6,405)*	*(5,857)*	*(5,517)*
2 Gross Profit	458	707	356	303
a Operating Expenses	(153)	(201)	(163)	(168)
3 Operating Profit	305	506	192	135
a Non Operating Income	*34*	*(5)*	*7*	*27*
4 Profit or (Loss) before Interest and Tax	339	501	199	162
a Total Finance Cost	*(93)*	*(182)*	*(144)*	*(102)*
b Taxation	*(69)*	*(109)*	-	*(2)*
6 Net Income Or (Loss)	178	210	55	58
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*423*	*683*	*406*	*311*
b Net Cash from Operating Activities before Working Capital Changes	*309*	*545*	*301*	*230*
c Changes in Working Capital	*334*	*(289)*	*37*	*(379)*
1 Net Cash provided by Operating Activities	643	256	338	(149)
2 Net Cash (Used in) or Available From Investing Activities	64	(237)	(91)	(1,139)
3 Net Cash (Used in) or Available From Financing Activities	(805)	(72)	(94)	1,185
4 Net Cash generated or (Used) during the period	(98)	(53)	152	(103)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-13.7%	14.5%	6.7%	11.7%
b Gross Profit Margin	9.9%	9.9%	5.7%	5.2%
c Net Profit Margin	3.9%	3.0%	0.9%	1.0%
d Cash Conversion Efficiency (EBITDA/Sales)	10.2%	10.4%	7.2%	6.1%
e Return on Equity (ROE)	20.4%	19.5%	5.6%	6.0%
2 Working Capital Management				
a Gross Working Capital (Average Days)	74	64	61	52
b Net Working Capital (Average Days)	67	58	54	44
c Current Ratio (Total Current Assets/Total Current Liabilities)	2.9	3.6	3.6	3.4
3 Coverages				
a EBITDA / Finance Cost	5.3	4.2	3.3	3.8
b FCFO / Finance Cost+CMLTB+Excess STB	1.4	1.5	1.2	1.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.3	3.3	6.3	8.4
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	62.7%	70.0%	73.2%	74.2%
b Short-Term Borrowings / Total Borrowings	0.3	0.4	0.4	0.3
c Average Borrowing Rate	5.1%	6.4%	4.9%	3.4%

Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

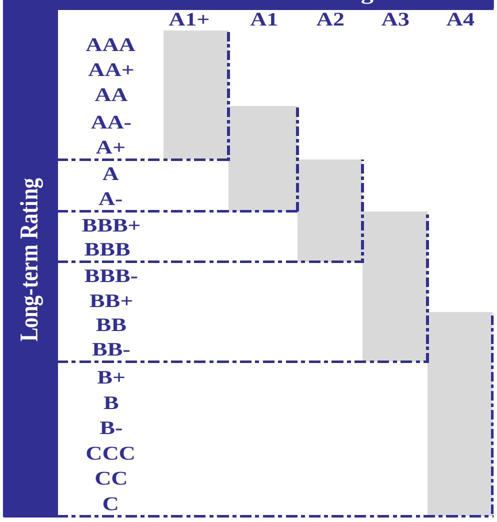
Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.

Short-term Rating



The correlation shown is indicative and, in certain cases, may not hold.

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities
a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
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(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
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